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### The Capital Connection

*The Capital Connection*, a bi-monthly publication from the Government of the District of Columbia Department of Insurance, Securities and Banking, will replace the agency's former newsletter, *The Financial Gateway Express*. It is done in-house by the department's Office of Communications. For more information, visit its Web site at [www.disb.dc.gov](http://www.disb.dc.gov). Please feel free to forward this newsletter to colleagues and other interested parties. If you would prefer not to receive this publication, contact Michelle Phipps-Evans at 202-442-7822 or send an e-mail to [michelle.phipps-evans@dc.gov](mailto:michelle.phipps-evans@dc.gov). Type REMOVE in the subject line.

## Consumer Corner

### DISB LAUNCHES LOCAL CAMPAIGN AGAINST FRAUD DURING FRAUD AWARENESS WEEK

By Michelle Phipps-Evans

**T**he Government of the District of Columbia Department of Insurance, Securities and Banking (DISB) launched the local fight against fraud in an information-driven campaign during Fraud Awareness Week, from July 9 to 14. The agency joined the Association

of Certified Fraud Examiners (ACFE), a global association dedicated to the worldwide fight against fraud, in sending out information on fraud prevention, detection and protection.

"Fraud affects everyone and its impact is felt worldwide," said DISB Commissioner Thomas E. Hampton  
*(continued on page 5)*

## CAPTIVE IN THE CAPITAL

### D.C. DEPUTY MAYOR

### STANLEY JACKSON IS KEYNOTE AT CIC-DC CONFERENCE

**T**he Captive Insurance Council of the District of Columbia, Inc. (CIC-DC) will feature the District's Deputy Mayor for Planning and Economic Development, Stanley Jackson, as its keynote speaker for this year's conference. Jackson will address the "Economic Development and Captives in the District of Columbia" at CIC-DC's fifth annual conference, *Managing Risk in the Alternative Market*, from Sept. 25-26, 2006, at the Marriott Metro Center.

Jackson has held various positions during his 23-year public service career. As Deputy Mayor, he is responsible for coordinating, planning, supervising, and in some cases executing all programs, policies, proposals and functions related to economic development in the District of Columbia. Jackson also advises the mayor on the most effective allocation of public resources devoted to economic development.

Some of the topics that will be covered at the conference are Offshore Captives Onshore, the GAO Report on Risk Retention Groups - One Year Later, GAAP vs. SAP Accounting-The



**Deputy Mayor Stanley  
Jackson**

Real Story, Using a Captive, the Effective Use of Reinsurance (case studies), DISB's perspective, and updates on new D.C. captive law. The conference will offer a high-caliber educational program designed to bring attendees up-to-date with the latest developments and issues making an impact on the captive insurance industry.

CIC-DC was founded in November 2001, and represents the corporate and association community interested in operating captive insurance companies in the District of Columbia, one of America's newest, and now leading domiciles for captives. For more information, visit CIC-DC's Web site at [www.dccaptives.org](http://www.dccaptives.org). \*\*\*

## DISB's Open House Touches Hot Insurance Issues



Commissioner Thomas E. Hampton introduces DISB's senior staff while giving opening remarks during the open house.

At DISB's all-day Insurance Open House on July 21, more than 40 compliance professionals and company representatives walked away knowing a little more about the District agency that regulates insurance, securities and banking.



DISB's legal team led an early morning session on legal questions and answers. They are back row, (L-R), Adam Levi, Lilah Blackstone, Leslie Johnson, Mary E. Lofton-Manning. Front, (L-R), Barry Kreiswirth, Supervisory Attorney-Advisor Rhonda Blackshear, Stephen Taylor and Michelle Mathis.

Although it was a full day of regulatory discussion, by the close of the day, many of the attendees were complimentary and glowing in their opinions about their experiences. Some said that since they spoke often on the phone to DISB staff, it was good to put a name to the face. Others thought that the topics were interesting, while many complimented the staff on its professionalism and knowledge.

***"This session was very helpful. I really appreciate all the hard work it took to get it together, and allowing us to interrupt your day."—an attendee at the open house.***

"I enjoyed the open house. I learned a lot to help me with my D.C. product," wrote one attendee.

"This is a wonderful venue. I am a health insurance broker representing 1,200 employee groups and I want to be a resource to help with this industry. Thank You," chimed another.

"This session was very helpful. I really appreciate all the hard work it took to get it together, and allowing us to interrupt your day. Thanks," echoed a third in written evaluations.

Some suggested that for next year's open



Director of the Enforcement and Investigation Bureau Stephen Perry poses before the start of the fraud compliance session.

house, DISB needs to discuss at length what it sees as emerging issues. This first-of-a-kind open house, hosted by the Insurance Bureau, was comprehensive in its content, surpassing the expectations of many.

The insurance compliance professionals, doing business in the District, attended concurrent sessions to learn about fraud



Insurance Examination Manager, Forms Analyst Branch, Jamaï Fontaine spearheaded the Insurance Open House.

compliance, producer licensing, new legislation in the insurance industry and prompt pay. They also learned about hot issues in the industry such as insurance for acts of terrorism or TRIA, about market conduct, form and rate filing requirements and dealing with consumer complaints. They also had a guided tour of DISB's main office at 801 First St., NE, where they met with various staff members who gave synopses of what they do.

Insurance Examiner Manager, Forms Analysis Branch, Jamaï Fontaine who spearheaded the open house, said she was

able to give attendees information based on what each division saw as crucial.

"The topics were the decision of each department," Fontaine said. "Each department decided on what it wanted to present."

Commissioner Thomas E. Hampton kicked off the program by assuring industry professionals that as government regulators, DISB believes in transparency, which is critical to sound and effective regulation.

"Your questions and input will help us in our constant drive to improve our efficiency as a regulatory agency," said Hampton, adding that the open house provided the opportunity for the regulator and the regulated to exchange ideas and close the communication gaps. Deputy Associate Commissioner of Insurance Luther Ellis and Stephen Perry, the head of the Enforcement and Investigation Bureau, also welcomed



Insurance Operations Manager, Consumer Service Division, Florence Thomas (in white) leads the discussion on consumer complaints and inquiries.

guests. The Associate Commissioner of Insurance Philip Barlow closed the day's event with remarks.

The day turned out to be a highly positive experience with all the presenters and those assisting with the open house, working doubly hard and feeling energized. One attendee aptly summarized the day's experience as "top notch," and "very well-planned," which was the consensus at the end of the day. \*\*\*



Insurance Examination Manager, Market Conduct, William McCune discusses market conduct issues with the audience.

# DISB NEWS BRIEFS



(L-R) Fire Marshal Richard Fleming, Donna Leaman of Allstate Insurance Company, DISB Commissioner Thomas E. Hampton, D.C. City Councilmember Phil Mendelson and DCIF director Larry Berman pose with the resolution from the D.C. Council.

## DISB joins forces with DCIF and FEMS

The D.C. Department of Insurance, Securities and Banking (DISB) joined the District of Columbia Insurance Federation (DCIF) on June 27 to help assemble fire safety kits for a charity program organized by DCIF designed to give away items that protect all District residents. DCIF joined forces with the Fire and Emergency Medical Services Department to get people more aware about safety precautions when it comes to fires in the home by assembling and donating 500 fire safety kits.

"Last year, we gave away smoke detectors," said Donna Leaman, who organizes the program, and is with Allstate Insurance Company. This year, residents will receive home fire extinguishers, smoke detectors (and replacement batteries), safety plug outlets, flashlights, a first aid kit, and other items to help prevent household accidents in a handy red tote. DCIF members Allstate, Liberty Mutual, Erie Insurance, USAA and Prudential Financial, who were on hand for the June 27 event, contributed more than \$13,000 to the program.

DISB Commissioner Thomas E. Hampton said he was pleased to see that the insurance industry is going beyond its call of duty for the District.

"I am glad that DCIF put this event together," Hampton said. "We can track risk to the insurance companies but it's better for us to teach people about risk avoidance and risk negation." Fire Marshal Richard Fleming said that the kits will be given out on a first come first served basis. Aleazor Taylor, a Juvenile Fire Settler Counselor in the Office of the Fire Marshal said that everyone who receives a kit has to spend about 30 minutes in a class learning how to use the equipment.

"To date, we have given out 17 kits," said Taylor, who added that they had a class in early August. "We are definitely hoping

for more citizens. It's very important to us that people who have these know how to use them." Also on hand at the June 27 event was Councilmember Phil Mendelson who recited the resolution adopted by the Council of the District of Columbia expressing its thanks to DCIF for the charitable safety kit donation.

*For more information on receiving a fire safety kit, call Patricia Everett at (202) 727-3296.*

## DISB's Securities Advisory Committee

Several times a year, DISB's Securities Advisory Committee (SAC) meets with director of Securities Theodore Miles and other senior staff to discuss matters of mutual concern between the industry and local regulators. Committee members are appointed by Mayor Anthony Williams to staggered terms. The current membership of SAC is chair, Frederick Douglass, Esq.; Isaiah Baker, Esq. (alternate); Michele Kulerman, Esq.; Jack Reutemann; Stanley Sporkin, Esq.; Theodore Urban, Esq.; and Lenda Washington. SAC held its last meeting in May, during which it discussed marketing hybrid products (insurance and securities in a package), and Special Purpose Acquisition Corporations, among other issues. The next meeting has been set tentatively for October.

## DISB marks milestone fifth anniversary of Securities Act of 2000

June 1, 2006, marked the fifth anniversary of the implementation of Titles III and IV of the District of Columbia's Securities Act of 2000, D.C. Official Code, Title 31, Subtitle X, Chapter 56, Subchapters III (Registration of Securities) and IV (Exemption From Registration). Those titles provide for registration and notice filings of certain securities offerings in the District of Columbia. The act, which was passed by the Council of the District of Columbia on July 11, 2000, was signed into law by Mayor Anthony Williams on Aug. 11, 2000. The law became effective Oct. 26, 2000. Its purpose is to protect investors and maintain public confidence in the securities markets while avoiding unreasonable burdens on participants in the capital markets. Applicability of Titles III and IV, requiring registration and notice filing of certain securities offerings in the District of Columbia began on June 1, 2001. Over the past five years since its implementation, about 101,465 registrations and notice filings have been recorded in conformity with Titles III and IV. During that period,

DISB's Securities Bureau has collected nearly \$69 million in fees for registrations and notice filings. The Securities Bureau has also issued four orders for violations of Title IV of the law during that time.



DISB Commissioner Thomas E. Hampton is flanked by former DISB Commissioner Lawrence Mirel (left) and former DISR Commissioner Robert M. Willis at a reception during the NAIC summer meeting.

## DISB hosts NAIC's 135th anniversary summer meeting

More than 1,700 insurance commissioners, producers, licensing personnel, examiners and others from around the nation, converged in the District of Columbia for the 135th anniversary of the National Association of Insurance Commissioners (NAIC)'s summer meeting in early June. DISB hosted the event at the Marriott Wardman Park Hotel.

"DISB is extremely excited about hosting this event, and having this national organization in our capital city," said DISB Commissioner Thomas E. Hampton. "After years of urban revitalization, Washington is at its best as a world-class city with rich local flair." Attendees participated in plenary sessions, workshops and task force meetings on various topics pertaining to the insurance industry. DISB also had an exhibit booth for staff to distribute insurance materials, tourist information and promotional items.

Based in Kansas City, Mo., NAIC is the coordinating body of the chief insurance regulatory officials of the 50 states, the District of Columbia and five U.S. territories. Its objective is to help state insurance regulators in consumer protection and to help maintain the financial stability of the insurance industry. Hampton delivered welcome remarks at the opening session on behalf of Mayor Anthony Williams. The District of Columbia Insurance Federation (DCIF) and the Property and Casualty Insurers of America (PCIA) honored Hampton as DISB's new commissioner at its reception on June 12.

"We're here to congratulate [Tom], said Larry Berman, executive director of DCIF. "I'm sure you'll all agree with me that [he] will make an impact."

*(continued on page 5)*

**D**ISB continues its showcase of the different bureaus or offices and its director. This month's newsletter features the Insurance Bureau.

## Philip Barlow and the Insurance Bureau

**P**hilip Barlow came to the then-Department of Insurance and Securities Regulation (DISR) in April 2000 as the Assistant Director for Financial Examinations. In that position, he oversaw the financial and actuarial components of the Insurance Bureau. In July 2005, he was selected as the Associate Commissioner of Insurance as part of a reorganization of the agency when DISR merged with the Department of Banking and Financial Institutions (DBFI). The merger created the Department of Insurance, Securities and Banking (DISB) when Mayor Anthony Williams signed legislation in 2004 that eliminated the walls of separation between the regulation of insurance and the regulation of banking. It was a direct result of the Gramm-Leach-Bliley law enacted by the U.S. Congress in 1999.

Barlow is a Fellow of the Society of Actuaries and a Member of the American Academy of Actuaries. Before joining DISB, he had worked for 16 years in the insurance industry. He started his career with the American Bankers Insurance Group in Miami, Fla., as an actuarial student. He later moved to the Acacia Mutual Life Insurance Company in Washington D.C., where he rose to the position of vice president and actuary. Barlow earned a bachelor's degree in business administration from Georgia State University with a major in actuarial science.

Unlike other bureaus at DISB, there is very little federal regulation of insurance, and there is no specific federal agency designated to oversee the activities of insurers and insurance producers. Insurance is predominantly regulated by the states and the Insurance Bureau works closely with the National Association of Insurance Commissioners (NAIC) to help create a uniform standard of insurance regulation across the country. NAIC is a voluntary organization of the chief insurance regulatory officials of the 50 states, the District of Columbia and five U.S. territories. Barlow is the chair of the NAIC's Life Risk Based Capital Working Group, and has spoken about risk-based capital at numerous NAIC and actuarial conferences. He has also traveled to Hyderabad, India, in 2004 and to

Cairo, Egypt, in 2006 on behalf of the NAIC to make presentations to regulators in those countries about U.S. risk-based capital.

The Insurance Bureau is the largest bureau at DISB and comprises seven branches – Actuarial, Consumer Services, Financial Analysis, Financial Examination, Forms Analysis, Market Conduct and Professional Services. Deputy Associate Commissioner of Insurance Luther Ellis assists in overseeing all the bureau's activities. Ellis brings more than 41 years of insurance and securities sales, management and regulatory experience to the agency, split almost evenly between insurance regulation and work in the private sector of the insurance industry. Ellis is a Fellow, Life Management Institute. He was awarded the 2004 Cafritz Award for Distinguished D.C. Government Employees for his exceptional leadership, remarkable dedication and outstanding services to the citizens of Washington, D.C.

There are more than 1,300 insurance companies and 43,000 insurance producers authorized to operate in the District of Columbia and they are all licensed by the Professional Services branch under the direction of Zandie Bowles. Bowles and her staff license and renew both the companies and producers operating in the District, oversee the appointment of the producers, and monitor compliance with continuing education and other requirements. Recently, Professional Services has actively moved to modernize the licensing process, so that much of the work can now be done online by the insurers and producers. This has greatly improved the flow process between DISB and its clients.

In addition to licensing, many of the policy forms and rates used in the District of Columbia are required to be filed and reviewed or approved by DISB. These tasks fall to the Forms Analysis and Actuarial branches. Almost all policy forms must be approved before they are used in the District of Columbia and this job is done by Jamie Fontaine and the staff of Forms Analysis. Rate review is slightly more complicated. Some products require prior approval of rates; some rates are filed and may be used until DISB takes issue with them; and some rates are not required to be filed at all. The Actuarial branch, under the direction of Robert Nkojo, is responsible for this. The agency participates in programs to help streamline the filing process and hopes



Associate Commissioner of Insurance  
Philip Barlow

to become part of the Interstate Compact that will significantly reduce the effort by insurers to get products approved in all states.

Financial solvency of insurance companies is a major focus of the Insurance Bureau, and the NAIC has developed a system through which each state has primary responsibility for monitoring the financial solvency of the companies domiciled in its state. For the District of Columbia, this responsibility rests jointly with the Financial Analysis and the Financial Examination branches. Insurance companies are required to file very detailed financial statements on a quarterly basis along with many other financial filings throughout the year. David Palmer and the Financial Analysis branch review all the filings for the domestic companies in the District. To ensure the completeness and accuracy of the financial information filed by the insurers, the Financial Examination branch, under Sean O'Donnell, conducts periodic audits of the District's domestic companies.

All states operate under the same system, and to verify that each state conducts financial surveillance to appropriate standards, the NAIC reviews and accredits each state every five years. An experienced team comes in and does a thorough review of DISB's applicable laws and financial review process to ascertain that it meets the high standards. The department received a five-year accreditation renewal in December 2005.

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about DISB's focus on fraud. "Today, both business and government organizations face new challenges in the effort to detect, prevent and investigate fraud."

DISB's fraud awareness campaign kicked off July 7 with a media and public outreach blitz where Hampton discussed the different types of financial-services fraud on WJLA/NewsChannel 8 with an anchor on a live news-talk program. He also discussed the issues on Telemundo 64, a Spanish-language television station, as well as with a reporter at *Asian Fortune*. Furthermore, Stephen Perry, the director of the Enforcement and Investigation Bureau (EIB), was interviewed live on WPFW 89.3FM on the measures his bureau has taken in detecting and preventing fraud.

Mayor Anthony Williams issued a proclamation declaring Fraud Awareness Week in the District, and his office ran a short article on DISB's efforts with the campaign in its bi-weekly electronic newsletter.

Beyond the media outreach, DISB instituted rigorous outreach efforts to inform the public about fraud. DISB's Office of Communications sent out daily newsletters to the media, community list serves and blogs on different types of fraud—insurance, securities and banking fraud, identity theft and EIB's brochure on fraud detection and prevention. Staff also handed out some of the information at the subway stops and in their own communities. Much of the news was timely especially in light of cases involving the number of stolen laptops with personal information.

This is the fourth year the District has participated in this national program sponsored by ACFE. State regulators and law enforcement agencies around the United States participate to highlight the problem and encourage the public to fight financial-services fraud. Financial fraud makes an impact on everyone on a daily basis. According to a 2004 Report to the Nation on Occupational Fraud and Abuse, U.S. entities lose more than \$600 billion



**Senior Insurance Operations Specialist Colin Van Niel hands out DISB information during Fraud Awareness Week at the Sidewalk Housing Fair, hosted by the Department of Housing and Community Development, on July 14.**

annually to fraud and abuse.

Insurance fraud is estimated as the number two fraud committed in the United States behind tax fraud. The National Insurance Crime Bureau estimated that the average American household pays \$300 a year in additional premiums to compensate for insurance fraud, for an estimated \$30 billion a year. Securities fraud continues to be part of our daily headlines and all citizens, particularly the elderly, are potential victims of a wide variety of securities fraud from false stock offerings to ponzi schemes (a type of illegal pyramid scheme). In the banking sector, DISB fights predatory lending, foreclosure scams, payday lending and unlicensed money transmitter fraud.

"We need citizens to fight back in the District and not tolerate any type of financial services fraud," Hampton said, citing statistics from the U.S. Department of Justice, which stated that only 15 percent of fraud victims report their losses to authorities. "DISB is encouraging more people to come forward. The purpose of Fraud Awareness Week is to equip residents with the tools so they can fight back by reporting any suspected type of financial fraud to DISB and put the criminals behind bars." \*\*\*

*Michelle Phipps-Evans is the senior public affairs specialist in DISB's Office of Communications.*

### **TOP TEN INSURANCE FRAUD SCAMS IN THE DISTRICT OF COLUMBIA**

- Staged auto accident fraud.
- Auto-owner-staged-car-theft-owner give-ups.
- Auto accident jump-ins. Insurance claim stating more riders in vehicle.
- Padded insurance claims regarding stolen property from vehicles and homes. Person adds more items to the claim than were actually stolen.
- False lost wages claims filed in auto accident claims.
- Agent, without the knowledge of individuals, signed them up for additional unwanted insurance coverage thus gaining additional commissions.
- Agent took payments from individuals but failed to purchase insurance for them.
- Medical providers fraudulently submitting billing of clients to insurance carriers.
- Persons continue working while illegally receiving long-term disability benefits and workers' compensation benefits.
- Persons staging slip and fall accidents.
- Auto premium avoidance fraud. District residents use false Maryland address to get cheaper Maryland insurance. The District government loses registration and license plate fees and insurers lose premium.

### **DISB and NAIC present health insurance gift to Mary's Center**

DISB and the National Association of Insurance Commissioners (NAIC) presented a charity gift of health insurance to Mary's Center for Maternal and Child Care in the Adams Morgan neighborhood on June 12 during the NAIC's summer meeting. The gift, which was donated by NAIC, will

provide aid to 56 low-income families. DISB Commissioner Thomas E. Hampton was on hand to make the presentation.

"Too many families in the District of Columbia lack basic health insurance, or access to care, and DISB is pleased that NAIC is lending a helping hand to mark its 135th anniversary and in recognition of its 56 members," said Hampton who suggested Mary's Center as the beneficiary of the gift as many DISB employees had given money to the center through the D.C. One Fund Drive, the District government's only

official charitable fundraiser. "I believe that Mary's Center will put the gift to good use for the families around the District." Mary's Center received a check for \$5,000 to enroll 56 new District families (one in honor of each state/territory) in health insurance and nutrition assistance programs. The center, which was established in 1988, aims to provide health care, education and social services for those in need. It strives to build better futures through the delivery of health care, education and social services, with a focus on District families who work in jobs where health insurance is not available. \*\*\*

## DISB Banking Bureau Protects and Serves

By Howard Amer

The Banking Bureau of the District of Columbia Department of Insurance, Securities and Banking (DISB) is the regulatory authority for financial institutions operating in the District of Columbia in all respects permitted by law. Through the Banking Bureau, DISB currently licenses more than 1,500 financial entities, and has chartered two commercial banks. The Banking Bureau ensures that financial institutions operating in the District provide financial services to the public in a manner that helps to meet the financial needs of the community.

DISB accomplishes this through licensing, examination and investigation of consumer complaints that the bureau receives about banks and the other financial institutions it regulates. In fiscal year 2005, the bureau processed 99 formal consumer complaints. Its average closure rate was 6.5 days, and 34 cases were submitted to the Enforcement and Investigation Bureau for review.

DISB's Commissioner Thomas E. Hampton is empowered to bring administrative action if there are violations of the law or regulations that the Banking Bureau administers, as well as to refer appropriate cases to the proper authorities for criminal prosecution.

In recent months, rising interest rates have slowed down; but in the last five years, they have made the home-buying market soar. Homeowners have been looking to upgrade their current homes, and many first-time homebuyers have only been able to afford to purchase homes with the assistance of the secondary market.

However, with an increase in home ownership, comes an increase in lending abuses and consumer complaints. A homebuyer should always seek the advice of an attorney or a professional consultant when buying or refinancing a mortgage to make sure that his or her rights are protected. Another way of ensuring protection is to use a lender that is licensed by the Banking Bureau.

The Banking Bureau recently received a complaint from a consumer who had some concerns regarding his mortgage refinancing. Because he had used a D.C.-licensed mortgage lender, the Banking Bureau was able to discuss the loan in question with the lender and identify the problems. As a result, the lender agreed to refund the customer \$1,500 of their closing costs. The constituent was impressed with the bureau's work.



Banking Bureau's Policy Analyst Evelyn Carmen presents information on financial services at a community conference in May.

This is just another example of DISB's Banking Bureau serving the District's community. Following is a letter addressed to Banking Bureau director, Howard Amer, about the incident.

*Dear Mr. Amer,*

*At the very end of last year we refinanced our home here in DC, thru (sic) (a lender) located in Atlanta, GA. To make a long story short – we felt that by the time we reached closing they had treated us unfairly and had done a “bait and switch” regarding the financing.*

*We contacted Evelyn Carmen in your office and she has just been wonderful and lovely to work with, which after living in DC for more than 20 years is something we rarely have had this positive experience with an employee of the DC Government. She acted on this promptly and her fast actions and “sticking” to what she also felt was not right resulted in a positive return to us from (the lender).*

*We felt it important to make you aware that I hope all your employees are as conscientious, dedicated and as pleasant to deal with.*

*Sincerely,*

*Jan Bradley and Thomas W. Morris III*

To check if the bank or financial institution you deal with is properly licensed in the District of Columbia, or to file a banking-related consumer complaint, please contact Evelyn Carmen at (202) 442-7849. \*\*\*

*Howard Amer is the director of the Banking Bureau.*

## District of Columbia to receive \$246,000 in Wachovia Settlement

Under the terms of a settlement announced in early July between state securities regulators and Wachovia Capital Markets LLC of Charlotte, N.C., the District of Columbia will receive \$246,000, including a \$30,000 credit for investor education upon final acceptance of the terms of the agreement, according to Commissioner Thomas E. Hampton of the Department of Insurance, Securities and Banking.

“This agreement is a major step in our ongoing efforts to help maintain investor confidence by ensuring that all investors are provided with objective research and treated with fairness and honesty,” Hampton said. The settlement results from allegations of potential conflicts of interest between Wachovia Capital Markets' research analysts and investment bankers. Hampton made the announcement following a 28-month investigation of the firm led by state securities regulators from Nebraska, Virginia and North Carolina, with assistance from Utah and Alabama, and contributions from Georgia, Maine, Connecticut and New Jersey.

The settlement effectively resolves a 28-month multi-state investigation of Wachovia Capital Markets, which operates Wachovia Corporation's institutional brokerage and capital markets businesses. The settlement, the allegations of which were neither admitted nor denied by Wachovia Capital Markets, includes the charges that Wachovia Capital Markets failed to supervise its employees in connection with potential conflicts of interest between equity research and investment banking as evidenced by research analysts' participation in certain presentations with potential investment banking clients. In addition, research analysts' evaluations sought information regarding their interaction with investment banking and the investment banking activity in their sector. Moreover, on occasion, Wachovia Capital Markets considered whether companies were potential clients in determining to provide research coverage on those companies.

In addition, Wachovia did not keep certain electronic communications as required by state securities laws. Wachovia Capital Markets' e-mail system and procedures were inadequate to ensure all electronic mail communications were retained and readily accessible. As a result,

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# The National Insurance Act

## THE WRONG APPROACH TO INSURANCE REGULATION IN THE UNITED STATES

By Dana Sheppard

There are two insurance bills pending in the U.S. Congress. The first is the State Modernization and Regulatory Transparency (SMART) Act of 2004, which was introduced by House Financial Services Committee chair Michael Oxley (R-Ohio) and Richard Baker (R-La.), chair of that committee's Capitals Markets Subcommittee. And the National Insurance Act of 2006, which was introduced by Senators John Sununu (R-N.H.) and Tim Johnson (D-S.D.), both members of the Senate Committee on Banking, Housing and Urban Affairs.

Both bills are intended to streamline insurance regulation, but take radically different approaches to that goal. The SMART Act would streamline state regulation by requiring states to develop and implement uniformity in the area of market conduct and rates. It would also establish a single-point-of-entry process for licensing insurance companies.

The National Insurance Act, on the other hand, would create an insurance regulatory system similar to the dual regulatory system found in the banking industry. The National Insurance Act would create a federal insurance commissioner who would have the authority to license and regulate national insurers and national agencies. States would still receive insurance premium taxes, and national insurers would still be required to participate in state guaranty associations.

The current state-based system of insurance regulation is inefficient and in need of major reforms. The only question is whether our future insurance scheme should be federally based or state based.

The approach taken by the drafters of the SMART Act is the better approach. It comes closer to requiring the states to adopt a single set of standards for all aspects of insurance regulation—not just solvency regulation. However, the SMART Act does not go far enough. Under the SMART Act, a national insurance company or producer would still have to deal with 51 regulators. Rather than simply requiring all states to adopt uniform insurance laws and regulations, it would be preferable to follow the state-led approach adopted in the federal Liability Risk Retention Act of 1986 (LRRRA).

The LRRRA's approach is preferable to the regulatory scheme currently envisioned in the National Insurance Act. The act has the support of the large national life, and

property and casualty companies (P&C), and large insurance brokers. The regional insurers and independent agents do not support it. Therefore, presumably there would still be numerous medium and small life and health, and P&C insurers, and producers licensed under a dual regulatory system. Unless uniform standards are mandated for all insurance regulation, a large segment of the insurance marketplace will continue to be regulated just as inefficiently as it is being regulated now. I see little point in undertaking such a major regulatory overhaul that still leaves the United States with an inefficient insurance regulatory system.

The drafters of the LRRRA created a very efficient regulatory process that could become the model for all insurance regulation in this country, but they have overlooked a deterrent to true state-led regulation. There are no enforcement provisions in the LRRRA, nor is there a federal insurance regulator or agency designated to enforce the LRRRA.

In theory, a risk retention group licensed under the LRRRA obtains a license in any one state or the District of Columbia, and it is then permitted to operate in any jurisdiction by filing its plan of operation in that jurisdiction. No license is required beyond the single license provided by the company's domiciliary regulator. The domiciliary regulator is responsible for all aspects of regulation, including licensing activities, solvency regulation and market conduct issues. Non-domiciliary jurisdictions have limited regulatory authority in cases where the non-domiciliary regulator has grounds to believe the company is operating in financially hazardous condition and the domiciliary regulator refuses to take appropriate action to remedy the problem.

In practice, however, several states ignore the federal preemptions of the LRRRA and require information and performance reviews of financial information, and engage in other activities, which clearly violate the LRRRA. Once a company is licensed by the domiciliary regulator under the LRRRA, it is simply required to register in any jurisdiction where it intends to conduct business by filing its plan of operation in that state. The operative word is filing. The non-domiciliary regulator is not supposed to review the filing, recommend or require

changes to the company's plan of operation, or ask for additional information such as rate information or policy forms. Most regulators follow the federal law, but several do not.

Risk retention groups frequently complain about blatant violations committed by some state insurance agencies, but rarely initiate litigation because of the considerable costs associated with challenging a state's authority in federal court.

Those states that impose the illegal requirements realize their advantage, and thumb their noses at the federal law. It should not come as a surprise to anyone who has been around insurance regulation for any time that state insurance regulators vigorously opposed the passage of the LRRRA. These violations could be stopped or significantly curtailed by amending the LRRRA to include language that would impose attorneys fees and punitive damages on states that violate the LRRRA. The SMART Act should be amended to include enforcement provisions that will deter states from not following the law.

Having worked with state-led insurance regulation, I believe that a state-based system is the better approach to insurance regulatory reform in this country. We already have experience with such a system, and it works reasonably well. An amalgamation of the lead-stated provisions found in the LRRRA with the uniformity requirements found mandated in the SMART Act would be an excellent model for future insurance regulation in the United States. \*\*\*

*The comments in this article are the personal views of the author, and do not represent the views of DISB's Commissioner Thomas E. Hampton, or DISB's official position.*

*Associate Commissioner Dana Sheppard is the head of DISB's Risk Finance Bureau.*



## **Wachovia Settlement**

*Continued from page 6*

20 percent of the e-mail folders requested in November 2002 could not be produced and 42 percent of the e-mail folders requested in January 2003 were not produced promptly. Wachovia Capital Markets also failed to maintain a system that allowed it to locate and retrieve back-up tapes for its e-mail system.

The multi-state settlement is related to the April 2003 Global Settlement that 12 other investment banks have reached with the state, federal and industry regulators. Under the terms of the settlement, Wachovia Capital Markets will pay a total of \$25 million, including \$20 million in penalties for failing to supervise its employees in connection with potential conflicts of interest between equity research and investment banking; \$1.65 million in penalties for failing to preserve required books and records; \$3 million to be used for investor education, as designated by the Board of Directors of the North American Securities Administrators Association Inc. (NASAA); and \$350,000 for costs associated with the investigation to be paid to NASAA.

Hampton added that the investigation

of Wachovia Capital Markets is part of a comprehensive regulatory effort to reform the relationship between investment banking and research and to manage appropriately conflicts of interest. The money received in the form of penalties will be paid into the General Fund of the District of Columbia. The District's share of the \$3 million dedicated to investor education will be paid to the Investor Education Fund of the Investor Protection Trust, a national non-profit organization based in Washington, D.C. \*\*\*



## **Insurance Bureau**

*Continued from page 4*

While all the functions mentioned above are important in protecting consumer interests relating to insurance, the last two branches deal most directly with the interactions between insurers and consumers in the District of Columbia. The Consumer Services branch, led by Florence Thomas, handles consumer complaints for any insurance policy issued in the District.

Thomas and her staff also promote consumer education for District residents to help prevent complaints from happening in the first place. William McCune and the Market Conduct staff review the way insurance products are marketed in the District to ensure that all such activities are done in accordance with District law.

Insurance products are becoming more complicated every day and have started incorporating features previously thought to be in the realm of banking or securities. There is much greater crossover among those people and businesses that sell insurance, securities and banking products. In addition, it is becoming more common for banks, securities firms and insurers to have a single parent. It is important to understand the overall operation of an organization for effective and efficient regulation. It has been a great benefit to the Insurance Bureau staff to work with the staff of the Banking and Securities bureaus in a coordinated fashion to provide effective regulation and protect the interests of all District residents. \*\*\*

*To contact the Insurance Bureau, call (202) 727-8000.*

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